

EXECUTIVE SECRETARIAT**ROUTING SLIP**

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		ACTION	INFO	DATE	INITIAL
1	DCI				
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Remarks

Executive Secretary
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Date

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ON FILE NSC AND COMMERCE RELEASE
INSTRUCTIONS APPLY

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THE WHITE HOUSE
WASHINGTON

85- 4313

CABINET AFFAIRS STAFFING MEMORANDUM

Date: 11/1/85 Number: 317,017 Due By: *Trade Strike*
Subject: Economic Policy Council Meeting -- Tuesday, November 5,
1:00 P.M. -- Roosevelt Room *Japanese Seminar*

ALL CABINET MEMBERS	Action	FYI		Action	FYI
Vice President	<input checked="" type="checkbox"/>	<input type="checkbox"/>	CEA	<input checked="" type="checkbox"/>	<input type="checkbox"/>
State	<input checked="" type="checkbox"/>	<input type="checkbox"/>	CEQ	<input type="checkbox"/>	<input type="checkbox"/>
Treasury	<input checked="" type="checkbox"/>	<input type="checkbox"/>	OSTP	<input type="checkbox"/>	<input type="checkbox"/>
Defense	<input type="checkbox"/>	<input checked="" type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Justice	<input type="checkbox"/>	<input checked="" type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Interior	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Agriculture	<input checked="" type="checkbox"/>	<input type="checkbox"/>	McFarlane	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Commerce	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Svahn	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Labor	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Chew (For WH Staffing)	<input checked="" type="checkbox"/>	<input type="checkbox"/>
HHS	<input type="checkbox"/>	<input type="checkbox"/>	Hicks	<input type="checkbox"/>	<input checked="" type="checkbox"/>
HUD	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Transportation	<input checked="" type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Energy	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Chief of Staff	<input checked="" type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
Education	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
OMB	<input checked="" type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
CIA	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Executive Secretary for:		
UN	<input checked="" type="checkbox"/>	<input type="checkbox"/>	DPC	<input type="checkbox"/>	<input checked="" type="checkbox"/>
USTR	<input checked="" type="checkbox"/>	<input type="checkbox"/>	EPC	<input checked="" type="checkbox"/>	<input type="checkbox"/>
GSA	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
EPA	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
NASA	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
OPM	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
VA	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
SBA	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>

REMARKS:

The Economic Policy Council will meet Tuesday, November 5, at 1:00 P.M. in the Roosevelt Room.

The agenda and background paper are attached.

RETURN TO:

☒ Alfred H. Kingon
Cabinet Secretary
456-2823
(Ground Floor, West Wing)

☐ Don Clarey
☐ Rick Davis
☐ Ed Stucky

Associate Director

THE WHITE HOUSE
WASHINGTON

November 1, 1985

MEMORANDUM FOR THE ECONOMIC POLICY COUNCIL

FROM: EUGENE J. McALLISTER *EM*

SUBJECT: Agenda and Papers for the November 5 Meeting

The agenda and papers for the November 5 meeting of the Economic Policy Council are attached. The meeting is scheduled for 1:00 p.m. in the Roosevelt Room.

The Council will consider a report from the Trade Strike Force. The Strike Force has prepared the attached papers addressing two issues: semiconductors and intellectual property. The issue of semiconductors concerns alleged unfair Japanese trade practices regarding predatory pricing and market access. The paper presents recommendations addressing each of those allegations.

The issue of intellectual property concerns how the Administration could strengthen intellectual property protection, both at home and abroad. The paper outlines a proposed comprehensive strategy addressing, for example, bilateral and multilateral negotiations, a legislative initiative, and a policy statement.

Confidential Attachment

THE WHITE HOUSE
WASHINGTON

ECONOMIC POLICY COUNCIL

November 5, 1985

1:00 p.m.

Roosevelt Room

AGENDA

- 1. Report of the Trade Strike Force**

CONFIDENTIAL**THE SECRETARY OF COMMERCE**
Washington, D.C. 20230

ON FILE NSC RELEASE INSTRUCTIONS APPLY

ON FILE COMMERCE RELEASE INSTRUCTIONS
APPLY

November 1, 1985

MEMORANDUM FOR THE ECONOMIC POLICY COUNCIL

FROM: Malcolm Baldrige, Chairman of the Strike Force

SUBJECT: Strike Force Recommendations on Semiconductors

ISSUE

The U.S. semiconductor industry is threatened by two kinds of alleged unfair practices by Japan:

- o Japanese dumping of semiconductors in the U.S. market.
- o Policies and practices which limit U.S. access to the Japanese semiconductor market, the second largest in the world.

The EPC is being asked to act on recommendations from the Strike Force on the strategy that the Administration should adopt to deal with these unfair practices.

STATUS AND IMPLICATIONS

Bilateral negotiations between the U.S. and Japan have addressed this situation over a number of years without success. As a result, U.S. industry has taken a number of actions under U.S. trade law.

- o A dumping charge on 64K RAMs, filed by Micron Technology
 - o A dumping charge on EPROMS, filed by Intel, Advanced Micro Devices (AMD) and National Semiconductor
 - o A Section 301 case filed by the Semiconductor Industry Association (SIA) claiming lack of market access in Japan and predatory pricing.
- ✓ In addition, two antitrust actions are in motion relating to Japanese predatory pricing practices in the U.S. market.

There is recent evidence that the newer 256K RAMs are also now being dumped on the U.S. market.

In the absence of equal access to markets and a restoration of fair pricing practices, it is likely that the United States semiconductor industry will be reduced to a very secondary role or eliminated as a significant factor in world competition. The impact on other U.S. industries that depend on this technology would be substantial if semiconductor manufacturing and applications skills were thus to be centered in Japan.

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RECOMMENDATIONS

The Strike Force recommends adoption and aggressive implementation of a program, already partly underway to counter the unfair aspects of this situation. Its elements include:

- ✓ 1. Prompt investigation and resolution of the two existing dumping cases. Self-initiation by the Department of Commerce of an antidumping case on 256K RAMs.
2. Support of USTR's accelerated plan for handling the existing 301 case. Support for consideration of a "package" proposal (addressing both market access and dumping) on semiconductors if such is put forward by the Japanese.
- ✓ 3. Announcement that the President will consider other remedial and/or preemptive actions to ensure U.S. access to Japanese markets.

BACKGROUND

(A more detailed paper describing the industry, its history and the commercial situation is attached.)

Overview

Semiconductors are the heart of computers, robots, industrial process controls, and other modern electronic devices, and the key to technological and cost leadership in many industries. Worldwide sales of semiconductors totalled \$25 billion in 1984. In 1984, the U.S. had a \$1.6 billion deficit in semiconductor trade with Japan.

After a long period of dominance in this technology, the U.S. now shares leadership with Japan and is falling behind in the newest generations of semiconductor products. Overall world market share is now 55% U.S., 35% Japanese, 10% others, with Japan in the lead on the newer products.

This condition results from Japanese targeting. Their strategy has been to exclude U.S. companies from their home market, while gaining share in ours by aggressive pricing policies. Japan has also expanded capacity rapidly; as a result, the industry is now oversupplied, and rapid price declines have taken place.

This year U.S. industry losses are estimated at over \$1 billion. United Technologies has liquidated its semiconductor (Mostek) division; Intel, AMD, and Natural Semiconductors have withdrawn from the RAM segment of the market. With the exception of captive manufacturers, U.S. firms are hesitant to invest in developing and producing the new high capacity products (1 megabit and 4 megabit chips) now on the drawing board, anticipating that Japanese practices will prevent such ventures from ever being profitable.

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History

In the 1960's, Japan used a ban on investment, high tariffs, and quotas to nurture its domestic semiconductor industry. Despite its comparative advantage, the U.S. was officially limited to no more than ten percent of the Japanese market.

In 1971, as a result of U.S. pressure, Japan agreed gradually to liberalize the industry by the end of 1974. But in 1975, MITI announced measures to "counter the liberalization." These included various subsidies, directives to buy Japanese, and government-sponsored joint R&D programs. A 1978 law continued MITI powers to develop and guide the industry. This law was replaced in mid-1985 by a new law for promotion of high-tech industries.

The U.S. market share has remained at 10 to 14 percent for many years, despite strong efforts by U.S. companies to expand in the Japanese market and their strong competitiveness elsewhere in the world. Half the market share that U.S. companies do have in Japan comes from one company's plant in Japan.

Recommendation 1 - Self-Initiate Antidumping Case on 256K RAMs from Japan

Texas Instruments is this?
agreed

U.S. law allows the Commerce Department to self-initiate antidumping cases. For antidumping duties to be imposed, Commerce must find dumping (U.S. sales below home market prices or below the cost of production) and the ITC must find injury to a U.S. industry.

Commerce investigation indicates that Japanese semiconductor companies are dumping 256K RAMs in the U.S. market by selling at less than their cost of production. Japanese 256K RAMs sell in the U.S. for \$2-2.50, while the fully allocated cost of production in Japan cannot be less than \$2.60 and may be as high as \$4.00. Commerce analysis also points to a probable injury finding by the ITC, based on substantial evidence of lost sales, major financial losses, massive layoffs, and U.S. companies exiting from the market entirely.

U.S. semiconductor producers that do not make 256K RAMs have filed AD cases on some types of semiconductors from Japan -- 64K DRAMs and EPROMs. The U.S. 256K industry strongly supports initiating a 256K RAM case, but fears repercussions in Japan if they are the petitioners. They are committed to cooperate fully in a case initiated by the USG.

Through an AD case, the U.S. industry wants to secure a change in Japanese pricing practices in the U.S. either by issuance of an antidumping order or by a negotiated solution leading to fair Japanese pricing. They expressly oppose any quantitative restriction on Japanese shipments of 256K RAMs to the U.S.

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In the case of EPROMs, Hitachi sent a letter to its distributors telling them to successively cut prices by 10 percent until they won the orders. Hitachi promised to guarantee the distributors' profit. This suggests that dumping may be endemic in all semiconductor markets.

PROS:

- Self-initiating a dumping case now would send a powerful message to both the Hill and our trading partners that we are serious about dealing with unfair trade. Such a step would also be a signal to the U.S. industry of USG concern and would encourage further effort by the U.S. industry in the next generation of products.
- Imposition of a dumping margin would provide relief to a hard pressed U.S. industry from a clearly unfair trade activity.
- Such a step would provide strong, GATT-consistent leverage for purposes of negotiating a better overall solution in the 301 case.

CONS:

- how strong in the case*
- A successful case would lead to at least a temporary increase in chip costs to U.S. users, who are now enjoying a windfall from the dumping. (However, semiconductors account for a small proportion of the final costs of most high-tech products.)
 - While the case looks strong, there is always some possibility that Commerce would not find dumping, or the ITC find injury.

~~Recommendation 2~~ Recommendation 2 -- Negotiate access and consider "package" deal

can we do this

The Semiconductor Industry Association's (SIA) filing of a 301 petition is the most recent step in a series of negotiations begun in 1982 by the US-Japan High-Technology Working Group over market access in Japan. This group negotiated two agreements that were approved by the Cabinets of both countries. These agreements committed Japan to providing access in Japan similar to that enjoyed by Japanese companies in the U.S. The Japanese government also undertook to encourage its companies to develop long-term relationships (as opposed to mere "spot" buying) with U.S. suppliers.

Throughout these negotiations, the SIA worked very closely with U.S. negotiators. When it became apparent in June that negotiations were

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not working, the SIA consulted with US negotiators about filing a 301 to put pressure on Japanese negotiators. The USG encouraged the filing with the intent of using it to negotiate better access.

The "package" concept was first suggested by Japan which wanted to trade something on access for a cessation of dumping and antitrust cases.

PROS:

- A negotiation leading to greater access in the Japanese market and a cessation of predatory pricing in the US market is what the industry has been requesting.
- Real market access is preferable to continued accusations of unfairness and retaliation.
- A dumping case would give leverage in the overall negotiating process.
- A package settlement allows the US and Japan as partners to avoid more drastic unilateral action.
- A "good" settlement would provide the basis for a "level playing field" in semiconductors.

CONS:

- Market access is undefined. Japan says the market is open and poor US results are due to lack of effort. No US negotiator believes that.

what could we expect

Essentially, we are looking for increased U.S. market share as evidence of an increase in access. But by how much? A deal inevitably leads to some, albeit tacit, agreement on market sharing.

- A package means some change in Japanese pricing policies. But of what kind and where? At a minimum we could ask Japanese companies to stop dumping in the US market, but to negotiate to get them to obey the law they should be obeying anyhow seems weak.

A meaningful pricing agreement would include cessation of sales below cost worldwide. But then are we negotiating a price cartel?

- Any settlement which does not halt the industrial policies that led to the problem in the first place is not likely to be meaningful. But no one believes Japan will ever halt these policies and practices.
- All semiconductor agreements with Japan in the past have failed. There is no mechanism here to ensure that this one would be any different.

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not agreed
Recommendation 3 -- Begin considering other steps.

This concept developed out of discussions at the interagency working level. All agreed that previous negotiations had failed to achieve equitable access. All agreed that the Japanese, if pressed sufficiently, might agree to a market-sharing agreement. All agreed that the US should not agree to market sharing. This meant, however, that a negotiated settlement would once again become a matter of relying on the GOJ to encourage its industry to buy more. All agreed that this would not work. There was a perceived need to give Japan an incentive to undertake to open the market.

PROS:

- The announcement of such consideration would be a powerful incentive to both the Japanese government and business to open the market.
- It puts the US in the position of being able to watch results and declare when it is satisfied, rather than becoming involved in sticky definitions of market access.
- It involves no irrevocable commitment.
- It begins to prepare us now for the possible eventuality that the Japanese will do nothing.

Cons

- It might complicate current negotiations.
- US users who rely on Japanese suppliers might become nervous.
- This could establish a precedent.

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OVERVIEW PAPER -- SEMICONDUCTORS

The Product

The electrical characteristics of semiconductors fall between those of insulators and conductors. This allows them selectively to store, generate, or process electricity as signals--that is, to handle information.

Silicon is the main semiconductor material. It is formed into thin, circular wafers, each divided into roughly 100 rectangular "chips". On each chip is etched a tiny pattern of circuitry that determines function and performance. Once complete, the wafer is tested and sliced into individual chips. The chips are then packaged in plastic and bonded to metal wires that plug the semiconductor into a larger electronic system (see "Applications" below).

Its Manufacture

The lines of circuitry printed on each chip are as small as one micron (1/1000 of a millimeter) wide. An individual chip, roughly 10 millimeters on a side, can contain 100,000 "gates" or circuit functions.

The manufacture of such precise structures requires technology ranging from an ultra-clean environment (since the smallest dust particle can incapacitate a circuit) to the highest-resolution optical equipment (to transmit complex designs from the "drawing board" onto the chip, error-free). A modern semiconductor fabrication plant can cost \$200 million.

Semiconductor Applications

Semiconductors are used in a variety of electronic equipment important to both service and manufacturing industries. They made possible the computer; they are the heart of telecommunications hardware and consumer electronic items (calculators, VCRs). They are the solid-state, microelectronics revolution that has so improved the performance of these products, miniaturized them, and reduced their cost.

Semiconductors now pervade our entire economy. In heavy industry, they enable robots to weld automobiles which rely on semiconductors for engine control, braking, passenger comfort. They precisely control oxygen flows and temperature conditions for steel plants. They provide the high-speed data handling and analysis on which our banking and insurance industries depend.

Semiconductor Types

The simplest semiconductors are called "discretes" because each chip has only a single electrical junction and can perform only one function. For example, a light-emitting diode--a discrete device used in electronic displays--can only be on or off, and its "choice" is determined by the incoming electrical signal.

Another type of discrete semiconductor is the transistor, which in 1948 launched the electronics age. Eleven years later, engineers placed several transistors onto a single chip--the first integrated circuit (IC)--to perform more complex tasks. Today, ICs dominate the semiconductor world. Progress in microelectronics now depends upon packing more and more transistors onto a single chip without sacrificing speed or consuming more electricity. The result is the miniaturization that we eventually see in more compact and powerful electronic products.

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There are two basic roles for an integrated circuit--memory or logic. Memory devices store information and return it on demand. Their primary features are their capacity and their response time. The 256K DRAM is a memory device that can store some 256,000 "bits" of data; most of these chips require less than 250 billionths of a second to access a stored cell. Although difficult to produce, they are standard, high-volume products, and the lessons learned from their manufacture are critical for production across a much broader range of devices.

Logic chips, on the other hand, process data. These include the "brains" of electronic systems, the microprocessor. The performance of logic chips is measured in terms of their speed per step and the amount of information (e.g., 16-bit) that they can handle at once. Their layout can be far more complex, and they are consumed in much smaller volumes than memories.

The US Semiconductor Industry

Historically, the US semiconductor industry has been the world's leader. Only five years ago, US manufacturers supplied some 65 percent of the world semiconductor market. Since then, they have lost roughly 10 points of market share to their Japanese competitors.

And 1985 has now brought the worst market conditions in over a decade--Japanese dumping, restricted access to their market, and a slump in computer demand will combine to drive US output down this year by 18-20 percent. This squeeze has hit independent American firms hardest because of the longer-term need to continue devoting tremendous resources to R&D and plant modernization. Despite the grim semiconductor business environment, chip-makers will spend over 10% of sales on R&D and another 25% of sales on plant and equipment in 1985.

Key Market Features

The long-term trend for semiconductor prices is down. This results from rapid technological progress in the lab and on the production line. Product lifetimes can be as short as 3 1/2 years. Over the last decade, the average cost per function dropped 17% annually. But in 1985, the final figure will fall between 35 and 40 percent.

This year's unusually steep decline was driven by some striking developments at the product level. The largest single market segment, random access memories (RAMs), was valued in 1984 at nearly \$6 billion. In 1985, another explosive increase in Japanese production capacity, stimulated by industrial targeting efforts, helped to drive prices of leading edge 64K and 256K dynamic RAMs down by over 80 percent.

But a presence in the memory market is critical for the US industry despite difficult competitive circumstances. Because companies manufacture here in greatest volume, this is where they can best advance their production and engineering skills. These capabilities are then transferred to other product segments. For this reason, memories are considered "technology drivers", fundamental to one's overall competitiveness in semiconductors.

*that
are
memory
plans*

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Nevertheless, the collapse of memory prices has induced most American companies to withdraw from the mainstream RAM market. Four firms dropped out with the previous (64K) generation. Only Texas Instruments, Micron Technology, and Motorola are likely to produce standard 256K DRAMs. AT&T manufactures primarily for internal use and has had difficulty marketing its device in the open market. IBM is strictly an in-house supplier, and even then it sources some 40% of its requirements from outside suppliers. Most US firms will now try to hold their ground in the other large memory field, electrically programmable read-only memories (EPROMs).

International Competition

For the US industry, semiconductor competition can be summed up in one word--Japan. The European market is significant, but features no domestic manufacturers of consequence. Japanese firms now supply 60 percent of world demand for the 64K DRAM and control 90% of the market for the latest device in this targeted product area. If current Japanese overinvestment and dumping practices continue, they will also dominate the coming 1-Megabit market.

As noted above, US exclusion from this market has serious implications for American companies' ability to compete in other areas. At the same time, the Japanese have begun to branch out from this base in commodity memory to attack more specialized memory products as well the logic field, two remaining areas of US leadership. Recent Hitachi dumping of EPROMs indicates that they will use this practice in their drive for market share in other segments as well.

The Japanese Strategy

collected and all set
The Japanese challenge in semiconductors was shaped by a concerted program of industrial targeting, aimed at a dominant world market position and similar to that used in shipbuilding and steel. This policy structure, and the economic/financial environment it fostered, encouraged the six major electronics firms in Japan to pursue semiconductor development aggressively. At the same time, it protected them from both domestic and international competition. Their initial concentration on core products and technologies is now spreading to a broader range of devices.

The Unfair Trade Practices--A History

The Japanese semiconductor program began in 1953 with passage of legislation that directed MITI to develop and implement a comprehensive promotion scheme. This included plans for creating an industry, providing financial support, suspending antitrust regulations, and coordinating R&D activity. For the next fifteen years, the Japanese market was formally protected by prohibitive quotas, tariffs, and foreign investment controls. Only Texas Instruments, in settlement of a Japanese violation of its semiconductor patents, was able to establish production in Japan, and even this occurred subject to MITI monitoring that limited its market share to 10 percent.

In 1974, the first market-opening measures were immediately neutralized by a "counter-liberalization" program, which included "buy-Japanese" provisions along with the continuation of subsidized research and inter-firm cooperation. By the late 1970s, more formal barriers had been lifted, but the legislation enabling government promotion was renewed and a landmark industry-wide R&D effort (the VLSI project) was launched with guidance and financing from MITI. This commercial project centered on dynamic-RAMs, now the competitive stronghold of the Japanese semiconductor industry. Typically, this product-specific focus, supported by the

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safety-net of protective legislation for depressed sectors, has encouraged overinvestment, overcapacity, and ultimately, dumping. (e.g., textiles, TVs)

Meanwhile, despite the ostensible openness of the Japanese market, US chips retained only a 10-15% share, frustrated by the vertically integrated and horizontally coordinated Japanese electronics establishment. In addition, only one-half of these semiconductor sales were actual imports; the rest came from US-owned production in Japan.

In 1982, negotiations began, aimed at improving US participation in the Japanese chip market, the world's second largest. The inability of US firms to compete with emerging Japanese rivals on the latter's home turf clearly weakened their overall strategic position, and by depriving US sales, raised total US production costs. Cabinet-level agreements, reached by the US-Japan High Technology Working Group, to pry open opportunities in Japan and refrain from illegal pricing practices were not implemented.

The Japanese pushed to export in greater volumes, and dumping became integral to their drive for market share in targeted product lines. As they gained production experience, the Japanese also focused more on upgrading their technological base. NTT continued to circulate its advances selectively to Japanese manufacturers. MITI organized new commercial research programs for semiconductor advancement--opto electronics, new materials, and microelectronics work for its 5th generation and supercomputer projects. And unauthorized Japanese duplication of semiconductor designs and processes, a problem early on for the inventors of the integrated circuit (Texas Instruments), arose again for American developers of the microprocessor as the Japanese industry sought to diversify into new product areas.

The Current Situation

Today, semiconductor trade frictions continue in both new and traditional forms. Negotiations continue (MOSS talks), yet the US share of the Japanese semiconductor market has fallen again to 10%, giving no indication that foreign access has improved. The Semiconductor Industry Association filed a 301 case directed at this problem; USTR plans a recommendation to the President in December. US firms have filed two dumping cases, both against Japanese memory producers. The Justice Department also began its own predatory pricing investigation of a Japanese semiconductor firm; a separate, private case was filed shortly thereafter.

The Implications for the United States

The fate of the US semiconductor industry will have far-reaching ramifications. It will directly determine our competitiveness across most high-tech industries, since semiconductors are their foundation. It will profoundly affect the capabilities of traditional manufacturers that have relied on electronics and automation to modernize facilities and maintain their business position. It will influence the cost effectiveness of our information-based service sector, from financial institutions to retailing. In addition, the entrepreneurship that has always characterized a healthy semiconductor industry attracts and cultivates a wealth of technical talent here in the United States, ensuring our position as a global technological leader.

Semiconductor-based electronics contribute directly to our economic efficiency and productivity as a nation. The growth, profitability, and employment that ensue are critical to our long-term economic well-being.

MEMORANDUM FOR: The Economic Policy Council
FROM: The Trade Strike Force
SUBJECT: Strengthening Protection for Intellectual Property

ISSUE

The violation of U.S. intellectual property rights--patents, trademarks and copyrights--is a serious impediment to U.S. international trade or competitiveness. An absence of laws in many countries, or the inadequate enforcement of existing laws, presents a barrier to American companies selling their products, and to establishing plants. What Administration steps would strengthen U.S. intellectual property owners' rights and secure more adequate foreign protection of U.S. intellectual property?

SUMMARY OF RECOMMENDATIONS

The Administration should pursue a comprehensive strategy that combines a legislative initiative with intensified ongoing efforts to combat foreign violations of intellectual property rights. The program would include:

- (1) an accelerated program of bilateral consultations on intellectual property and, where appropriate, consideration of additional Section 301 unfair trade cases.
- (2) continued efforts to improve multilateral disciplines on intellectual property through the new trade round, the OECD, and existing conventions on intellectual property (WIPO/UNESCO).
- (3) issuance of a policy statement on intellectual property that reflects the items above.
- (4) an Administration legislative initiative to close gaps in U.S. protection of intellectual property and to strengthen U.S. intellectual property owners' rights against infringers.
- (5) identification of ways in which existing treaties and U.S. laws can be used to secure adequate foreign intellectual property protection, including prompt notice to GSP countries of the progress they must make in protecting intellectual property in order to retain GSP benefits following the January 1987 GSP review
- (6) creation of an advisory committee on intellectual property rights, co-chaired by USTR and Commerce, to provide a formal channel for private sector advice.

BACKGROUND

Inadequate Foreign Protection

Theft of intellectual property rights is on the increase worldwide and causes an estimated lost U.S. sales of \$8-20 billion annually. Additional substantial losses result from restrictions on access to foreign markets by U.S. innovations. International violations of intellectual property rights have become rampant as communications and markets are now international and intellectual property has become key to high-tech trade.

Inadequate intellectual property protection access is particularly acute in, although not confined to, the NICs. It includes:

- o the absence of national patent, trademark, and copyright laws, (e.g., Indonesia).
- o patent laws that inadequately protect chemicals and pharmaceuticals (Taiwan, Korea, Brazil, Mexico and Canada).
- o copyright laws that provide uncertain or inadequate protection to U.S. works or which exclude or provide overly short-term protection for computer software (Korea, France).
- o inadequate implementation and enforcement (many countries).

These practices affect a wide spectrum of American industries including chemicals, pharmaceuticals, motion pictures, publications, semiconductors, computer software, apparel and other consumer goods, and new industries such as biotechnology.

- o RECOMMENDATION #1: That the United States pursue an aggressive, effective bilateral strategy to accelerate discussions with key countries. This has already been undertaken in accordance with a Presidential directive. We should also examine appropriate additional cases for Section 301 action.

Background: Piracy and counterfeiting have grown dramatically especially in the newly industrialized countries of the Pacific Basin and Latin America. Effective protection of intellectual property rights in most of these countries lags far behind that provided in nearly all developed countries.

For example, Korea's copyright laws do not protect foreign works or computer software and Singapore's do so only in limited circumstances. Indonesia has no patent law. Patent law in Korea and Taiwan does not cover chemicals and pharmaceuticals.

The U.S. has had a series of bilateral consultations with Latin American and Asian nations to remedy the problem. These consultations should be accelerated. Contacts should include: Korea, Taiwan, Brazil, Argentina, Yugoslavia, India, the Philippines, Mexico, Indonesia, Malaysia, Singapore and Thailand. Further consultations also should be held with Canada on its practices with respect to pharmaceutical patents, and France on its recently enacted overly short term protection for computer software.

If consultations fail to produce sound progress in a timely fashion, the Strike Force will consider whether the filing of additional 301 actions is warranted. We have already initiated a 301 case involving Korea.

- Pro:
- o Bilateral consultations would build on previous discussions which have resulted in some positive changes in foreign countries. This allows countries to address the problem and change practices before any action is taken.
 - o We have the precedent of initiating a 301 case on Korea. Further consultations with other offender countries should be undertaken before any additional action is taken.
- Con:
- o Bilateral packages would have to be consistent with current and proposed multilateral agreements, possibly diluting them because of inadequate minimum standards at the multilateral level.
 - o Some Section 301 cases might be challenged through the GATT.
 - o Countries will probably react negatively to Section 301 actions.
 - o Excessive use of 301 by the Strike Force could overload USG circuits and diminish our ability to bring these cases to a successful conclusion.
- Just Summary?*
- o RECOMMENDATION #2: That the Administration increase efforts aimed at securing multilateral protection of intellectual property rights through: including the topic as a priority in a new round of trade negotiations; vigorously pursuing ongoing efforts to improve existing conventions; and expanding OECD work on the issue.

Background: The GATT, while addressing intellectual property in four areas, does so on an exception basis. Existing multilateral discipline comes through a number of other international agreements, including the Paris and Berne Conventions, administered by the World Intellectual Property Organization (WIPO), and the Universal Copyright Convention, administered by UNESCO. These agreements center generally on ensuring national treatment and establishing some minimum standards for the holders of intellectual property rights, but they lack a proven mechanism for resolving disputes. Despite the existence of international conventions, violations of intellectual property rights have become rampant. Ongoing efforts to improve existing conventions should be pursued vigorously, e.g. WIPO's work on semiconductor chip protection and biotechnology.

Efforts have been underway in the GATT since the end of the Tokyo Round to conclude an Anticounterfeiting Code, which have intensified since the November 1984 Contracting Parties meeting. These efforts need to be expanded in the new round context. As a first step, the U.S. should take the lead in seeking to form a "Friends of Intellectual Property" group in the GATT to advance consideration of the issue in the New Round.

Multilateral efforts should continue in other arenas as well, such as investigating efforts to include intellectual property in the coverage of the Invisibles Code in the OECD.

- Pro:
- o Would signal multilateral commitment to the issue and would supplement bilateral initiatives.
 - o Would bring intellectual property disputes in the trade area into the clear purview of the institution charged with addressing trade disputes, the GATT.
 - o Would build on over 100 years of effort internationally, for instance the Paris Convention was adopted in 1883.
- Con:
- o Multilateral solutions are by their nature slow and deliberate. They do not show immediate results as do bilateral initiatives. Thus they would not be responsive to the short-term concerns of the business community or Congress. Multilateral efforts need to be supplemented by bilateral and unilateral actions aimed at short-term remedies.

- o **RECOMMENDATION #3:** That the Administration issue a policy statement on intellectual property.

Background: Such an action is supported by industry and labor. A policy statement would provide a focal point and a touchstone for the implementation of the programs described in this document, similar to the previous Administration trade and investment policy statements.

There is, however, an issue of timing relating to the issuance of a policy statement which the EPC should address.

Option 1: The Strike Force should be directed to produce a policy statement within a week's time for issuance by the Administration. Such a statement would incorporate the initiatives included in this paper and private sector advice received to date.

- Pro:** o Would show our determination to move quickly on this issue and put other countries on notice as to the priority the Administration attaches to it.
- o Would provide a useful vehicle for organizing the various elements of our initiative into a comprehensive program.
- Con:** o Moving on this fast timetable would preclude our systematically seeking private sector advice, a process which proved useful in the development of past policy statements, e.g. the 1983 investment policy statement.

Option 2: As indicated in the attached Action Plan, the Strike Force would be directed to produce a policy statement within 4-6 weeks time.

- Pro:** o Would allow for extensive consultation with industry and on an interagency basis, thus producing a statement which reflects a broad consensus of views.
- Con:** o May give the appearance of delaying action on the intellectual property issue.

- o **RECOMMENDATION #4:**

- o (A) That the Administration introduce an Administration bill amending domestic law to strengthen intellectual property protection for U.S. producers. Alternatively, the Administration could announce active support for intellectual property legislation introduced on the Hill.

- Pro:** o Would put us out in front on the issue and make clear that this is an Administration priority.
- o Would gain faster action on proposals we have supported for some time.

- Con: o Would introduce the risk that the bill could be put into legislation the Administration does not support, creating problems for Presidential action.
- o (B) The legislation would contain the following provisions:
- Amend Section 337 of Tariff Act of 1930 to delete injury test and necessity to show that the domestic industry is economically run.
 - Extend patent protection to cover products of patented processes.
 - Extend life of agricultural chemical patents to compensate for time lost due to regulatory processes. (This was done for pharmaceuticals in the 98th Congress.)
 - Subject aspects of patent licensing arrangements to "rule of reason" in antitrust cases instead of "per se" rule.
 - Increase procedural safeguards to prevent inappropriate release of privately-owned proprietary information held by the Government.

Background: These provisions have already been approved in the legislative package.

- Pro: o Would remove burdensome administrative requirements that hamper the effectiveness of existing statutes (particularly in the case of Section 337).
- o Would close loopholes now benefitting foreign producers at the expense of U.S. property rights holders (particularly in the case of current process patent law)
- o Would make U.S. law consistent in recognizing the need to compensate patent holders for the patent life lost due to pre-marketing regulatory clearance proceedings.
- o RECOMMENDATION #5: That the U.S. Government use existing laws and agreements more aggressively to ensure greater protection for U.S. holders of intellectual property rights worldwide. This could include prompt notice to GSP countries of the progress they must make in protecting intellectual property in order to retain GSP benefits following the January 1987 GSP review.

Background: We should examine existing bilateral treaties such as FCNs and BITs to determine whether any of the rights and obligations they create can be used to enforce the rights of U.S. owners of intellectual property rights. A failure to enact laws which enable a nation to live up to its treaty obligations, or using liberal definitions of such terms as "property" in existing treaties to include intellectual property, might be grounds for trade action. In addition we should examine the applicability of anti-expropriation provisions of various U.S. statutes in cases where foreigners impose compulsory licensing on American patent and copyright owners without prompt, adequate and effective compensation.

Perhaps the strongest incentive for positive change in developing and newly industrialized nations is the amendment of GSP in the 1984 Trade and Tariff Act giving the President increased authority to act to protect U.S. intellectual property rights under this program. New GSP provisions require consideration of a nation's treatment of intellectual property rights in the general review of continued eligibility for tariff concessions.

- Pro:
- o Would be a strong indication to our trading partners and the U.S. business community that we are serious about pushing for increased protection in this area.
 - o Notice to GSP countries that adequate intellectual property rights will be a significant review criterion could push infringer countries into making earlier and more fundamental changes.
 - o RECOMMENDATION #6: That the USG pursue formal lines of communication with the private sector through the Advisory Committee on Trade Negotiations (ACTN) working group on intellectual property rights and establish a private sector advisory committee on intellectual property rights co-chaired by USTR and Commerce.

Background: The business community and labor groups are strongly committed to improving intellectual property protection. The Presidentially appointed Advisory Committee on Trade Negotiations has formed a task force on intellectual property. This task force has split its work into two stages: first it will make recommendations to the full ACTN on multilateral approaches to trade policy, and then it will work to identify major bilateral initiatives and approaches. Their objectives are 1) higher norms, transparency and removal of current practices such as compulsory licensing; 2) adequate enforcement mechanisms; and 3) dispute settlement procedures.

- Pro:** o During the past year the Administration has informally worked with the private sector through individual companies, the ISACs and umbrella organizations established by U.S. industry on intellectual property rights. Work by the ACTN task force and a private sector advisory committee would complement these efforts.
- Con:** o Once communication is formalized, the business community may have false expectations on how quickly the USG can make changes.

- Attachments:** A. Timetable for Action Plan Initiatives
- B. Summary of Current U.S. Law and International Rules

Action Plan Dates

- a. Intellectual Property Policy Statement
Staff draft with private sector comments reflected:
December 1, 1985
- b. Action on Legislation Related to Strengthening Domestic Practices of Intellectual Property: Fall 1985
- c. Acceleration of Bilateral Negotiations
Target plan for Brazil/Mexico and other countries with IPR problems: December 1, 1985
- d. Review Obligations of Our Trading Partners Existing in Current Bilateral Agreements: December 1, 1985
- e. Review of Korea 301 Case and Consideration of Other Possible Immediate Intellectual Property-related 301 Actions:
January 1, 1986
- f. Completion of Full ACTN Report on Priority Countries and Issues for Consultation and 301 and GSP Action Programs:
February 28, 1986
- g. Review of Private Sector Report for Possible Section 301 Actions: March 1, 1986
- h. Initiation of GSP-related Review Based on Intellectual Property Criteria of Trade Act: Summer 1986

APPENDIX

Current U.S. Law

The Administration has favored certain improvements relating to intellectual property, e.g., process patents, firmware, chemicals, and patent misuse rules, and remedies against infringement,

U.S. intellectual property owners have two remedies against infringement:

- o Seeking damages and injunctions against infringers in federal courts. Because the courts must have jurisdiction over the infringer, this remedy applies chiefly to violations in the U.S.
- o Filing an unfair practice case under Section 337 of the Tariff Act of 1930. Under Section 337, the ITC may issue an exclusion order barring imports of items that infringe U.S. patents, trademarks and copyrights. To obtain relief, the petitioner must demonstrate that the import or sale of the infringing product substantially injures an industry that is efficiently and economically operated in the U.S.

International Rules

The GATT covers intellectual property only on an exception basis.

The effectiveness of existing international intellectual property conventions is in some cases limited due to lack of signatory countries, lack of minimum standards, lack of coverage, and lack of enforcement.

The Paris Convention on patents and trademarks provides for national treatment and priority for filing dates, but generally does not set minimum levels of protection.

For copyrights, the Berne Convention provides for national treatment and generally a minimum copyright term of the author's life plus 50 years. (The U.S. is not a signatory, but the Administration has supported joining.) The Universal Copyright Convention (UCC), to which the U.S. is signatory, provides for national treatment and a term of the author's life plus 25 years. Both the Berne and UCC contain substantial minimum standards. Significant countries (e.g., Korea, Indonesia) are signatory to neither copyright convention.